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Message Text

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ACTION EUR-12

INFO OCT-01 EA-07 IO-11 ISO-00 AID-05 CIAE-00 COME-00

EB-07 FRB-03 INR-07 NSAE-00 USIA-06 TRSE-00 XMB-02

OPIC-03 SP-02 CIEP-01 LAB-04 SIL-01 OMB-01 NSC-05

SS-15 STR-04 CEA-01 PA-01 PRS-01 /100 W
---------- 029839
R 031732Z FEB 76
FM AMEMBASSY LONDON
TO SECSTATE WASHDC 8679
INFO AMEMBASSY BERN
AMEMBASSY BONN
AMEMBASSY BRUSSELS
AMEMBASSY COPENHAGEN
AMEMBASSY DUBLIN
AMEMBASSY LUXEMBOURG
AMEMBASSY PARIS
AMEMBASSY ROME
AMEMBASSY STOCKHOLM
AMEMBASSY THE HAGUE
AMEMBASSY TOKYO
AMCONSUL BELFAST
AMCONSUL EDINBURGH
USMISSION EC BRUSSELS
USMISSION OECD PARIS
USDEL MTN GENEVA

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DEPARTMENT PASS TREASURY AND FRB

E.O. 11652: N/A
TAGS: ECON, UK
SUBJECT: WILSON REVIEWS ECONOMY IN SPEECH TO BANKERS

REFERENCE: LONDON 1414
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SUMMARY: THE PRIME MINISTER'S SPEECH TO THE OVERSEAS BANKERS CLUB RECOUNTED ENCOURAGING PROGRESS IN THE CONTAINMENT OF INFLATION, STRESSED THE GOVERNMENT'S CONTINUING RESISTANCE TO ANY MAJOR REFLATION TO REDUCE UNEMPLOYMENT, AND CONTAINED ASSURANCES THAT THE GROWTH OF PUBLIC EXPENDITURE WMULD BE CONTROLLED. END SUMMARY.

1. PRIME MINISTER WILSON REVIEWED RECENT DOMESTIC ECONOMIC DEVELOPMENTS AND DESCRIBED THE GOVERNMENT'S APPROACH TO UPCOMING POLICY DECISIONS IN HIS FEBRUARY 2 ADDRESS TO AN AUDIENCE OF LONDON REPRESENTATIVES OF OVERSEAS BANKS. HE TOUCHED ON THE NOW FAMILIAR THEME OF THE VERY REAL PROGRESS BEING MADE TO REDUCE THE RATE OF INFLATION NOTING THAT PRICES WHICH HAD BEEN RISING AT AN ANNUAL RATE OF 34.8 PERCENT DURING THE FIRST HALF OF 1975 ROSE AT AN ANNUAL RATE OF 14.1 PERCENT DURING THE SECOND HALF OF THE YEAR.

2. MR. WILSON, WHILE ENCOURAGED BY THIS PROGRESS, STRESSED HIS DETERMINATION THAT THERE BE NO EASING OF EFFORTS NOT ONLY TO BRING INFLATION DOWN TO LEVELS COMPARABLE TO THOSE OF BRITAIN'S MAJOR TRADING PARTNERS, BUT TO KEEP IT THERE. REFERRING TO THE RECENT SPATE OF DEMANDS TO PROVIDE RELIEF FOR THE RAPIDLY RISING NUMBERS OF UNEMPLOYED, MR. WILSON SAID "IT WOULD BE A GREAT MISTAKE TO ACT PRECIPITATELY AND REFLATE NOW ON A MASSIVE SCALE."

3. HE POINTED TO SIGNS THAT OUTPUT IS REVIVING BUT, LIKE THE CHANCELLOR OF THE EXCHEQUER IN THE PARLIAMENTARY DEBATE (REFTEL) ON EMPLOYMENT, UNDERLINED THAT LAGS WERE INEVITABLE BETWEEN THE UPTURN IN OUTPUT AND THAT IN EMPLOYMENT. IN THE INTERIM, HE SAID THAT SCOPE WAS AVAILABLE FOR FURTHER LIMITED MEASURES TO ENCOURAGE EMPLOYERS TO HIRE YOUNG PEOPLE, TO PROVIDE ADDED RESOURCES FOR RETRAINING, AND TO CREATE GREATER INCENTIVES FOR IMMEDIATE INVESTMENT. NEVERTHELESS, THE GOVERNMENT'S FREEDOM OF MANEUVER IS CIRCUMSCRIBED BECAUSE OF THE NEED TO FREE RESOURCES FOR INVESTMENT AND EXPORT.

4. TURNING TO THE LIKELYCOURSE OF PUBLIC EXPENDITURE,

MR. WILSON SAID THAT THE ANNUAL WHITE PAPER WILL REFLECT

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OPIC-03 SP-02 CIEP-01 LAB-04 SIL-01 OMB-01 NSC-05

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TO SECSTATE WASHDC 8680
INFO AMEMBASSY BERN
AMEMBASSY BONN
AMEMBASSY BRUSSELS
AMEMBASSY COPENHAGEN
AMEMBASSY DUBLIN
AMEMBASSY LUXEMBOURG
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NOT PANIC BUT A "RATIONAL LOOK AT THE CHOICES AND PRIORI-
TIES." HOWEVER, WITH INDUSTRY RUNNING FAR BELOW CAPACITY
AND HIGH UNEMPLOYMENT, HE BELIEVED THAT "IT WOULD HAVE
BEEN ECONOMICALLY IRRELEVANT, AS WELL AS SOCIALLY IRRE-
SPONSIBLE TO CUT PUBLIC EXPENDITURE FOR THE MONTHS IMMEDI
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ATELY AHEAD." HAVING RULED OUT CUTS IN THE PLANNED SPENDING LEVELS FOR THE 1976/77 FISCAL YEAR, MR. WILSON EMPHASIZED THAT BRITAIN COULD NOT REPEAT THE MISTAKES MADE DURING THE PAST BUSINESS CYCLES BY PERMITTING EXCESSIVE INCREASES IN PUBLIC CLAIMS ON LIMITED RESOURCES. THIS WOULD ONLY PLACE FURTHER STRESS ON AN INDUSTRIAL BASE WEAKENED BY YEARS OF RELATIVE DECLINE AND "CALLED ON TO PAY FOR A GROWING SUPERSTRUCTURE OF CONSUMPTION, BOTH PUBLIC AND PRIVATE."

5. COMMENT. THE TIMING OF THE WILSON SPEECH, COMING JUST AFTER THE PARLIAMENTARY DEBATE ON UNEMPLOYMENT AND PRIOR TO THE ANNOUNCEMENT OF DETAILS OF THE LIMITED MEASURES TO INCREASE EMPLOYMENT, APPEARS DESIGNED BOTH TO RIDE THE GROWING CONSENSUS THAT THE ECONOMY HAS TURNED THE CORNER AND TO DOWNPLAY A PREMATURE POUNDS AND PENCE DEBATE OF THE NEXT PHASE OF THE INCOMES POLICY.

6. EXTRAPOLATING FROM THE STATEMENT ON PUBLIC EXPENDITURE LEADS TO THE CONCLUSION THAT WITH UNEMPLOYMENT LIKELY TO REMAIN ON A HIGH PLATEAU THROUGHOUT 1976 AND NO CUTS IN PUBLIC SPENDING IN THE OFFING, THE GOVERNMENT'S BORROWING REQUIREMENT WILL CONTINUE TO MAKE LARGE DEMANDS ON CAPITAL MARKETS. THIS POSSIBILITY HAS PROVOKED THE FINANCIAL TIMES FOR ONE TO RESURRECT THE CROWDING OUT HYPOTHESIS WITH THE RISK OF HEAVY GOVERNMENT BORROWING KEEPING INTEREST RATES HIGH AND IMPEDING A RECOVERY IN PRIVATE INVESTMENT LATER IN THE YEAR.

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Message Attributes

Automatic Decaptioning: X
Capture Date: 01 JAN 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: ECONOMIC CONDITIONS, ANTIINFLATIONARY PROGRAMS, ECONOMIC REPORTS, SPEECHES, BANKERS
Control Number: n/a
Copy: SINGLE
Draft Date: 03 FEB 1976
Decaption Date: 01 JAN 1960
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Authority: GolinoFR
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 28 MAY 2004
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1976LONDON01711
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Film Number: D760040-1033
From: LONDON
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1976/newtext/t19760288/aaaaczn d.tel
Line Count: 200
Locator: TEXT ON-LINE, ON MICROFILM
Office: ACTION EUR
Original Classification: LIMITED OFFICIAL USE
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 4
Previous Channel Indicators: n/a
Previous Classification: LIMITED OFFICIAL USE
Previous Handling Restrictions: n/a
Reference: 76 LONDON 1414
Review Action: RELEASED, APPROVED
Review Authority: GolinoFR
Review Comment: n/a
Review Content Flags:
Review Date: 24 MAR 2004
Review Event:
Review Exemptions: n/a
Review History: RELEASED <24 MAR 2004 by ElyME>; APPROVED <24 MAR 2004 by GolinoFR>
Review Markings:

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US Department of State
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04 MAY 2006

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: NATIVE
Subject: WILSON REVIEWS ECONOMY IN SPEECH TO BANKERS
TAGS: ECON, UK, (WILSON, HAROLD)
To: STATE
Type: TE
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 04 MAY 2006